the platform have the ability to expand as demand increases so as to avoid becoming a bottleneck.[504] As we noted, these requirements (as modified here) will ensure greater diversity of video programming and further our goal of fostering the deployment of an advanced telecommunications infrastructure. Nevertheless, it has become apparent through the Section 214 application process that there may be technical limits on the expandability of analog capacity in video dialtone systems. To the extent digital transmission facilities can be used instead to deliver the same programming, capacity constraints are substantially mitigated. The economic and technical viability of digital capacity in the short term, however, is unclear for two reasons. First, there is uncertainty about the widespread availability and commercial feasibility of digital compression and transmission equipment. Second, if digital capacity is used for video dialtone, end user subscribers must have a set-top converter to view the video signals on today's televisions. Currently, the cost of a set-top converter is approximately $300.[505]

269. In its Section 214 application, GTE has proposed a video dialtone system that would make extensive use of digital capacity. GTE proposes a platform with approximately 168 compressed digital channels, 80 analog channels, and 4 reverse analog channels.[506] Programmer-customers on GTE's platform would have the option of delivering to GTE an analog signal or a digital signal. If a programmer-customer delivered an analog video signal, GTE would either modulate this signal onto an analog channel, or encode and multiplex this signal input onto a digital bit stream.[507] The analog signal or digital bit stream would then be delivered over the video dialtone network. To access all channels and services offered on the platform, GTE's proposal requires end user subscribers to purchase or rent a set-top converter, both because the converter is needed to view compressed digital video signals on today's televisions and because some channels may be encrypted.[508]

270. We now seek comment on the merits of the GTE approach or some variation of it as a way of meeting our capacity and expandability goals. Parties commenting on this approach should address, in particular, the technical, economic, and operational

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504 Second Report and Order at 5797, paras. 29, 30.

505 See SWBT ex parte letter, June 1, 1994, at 5.

506 GTE Section 214 Application, File No. W-P-C-6955, at 6 (May 23, 1994).

507 Id.

508 Id. at 9.

feasibility of digital equipment and facilities. For example, we seek comment on whether digital compression and transmission equipment will be commercially available on a broad scale in the near future, and on the quality of compressed digital video. We also seek comment on the costs of digital equipment. Likewise, we seek comment on the cost of set-top converters and on whether and when, given these costs, we should require LECs to employ all-digital video dialtone systems. In addition, we seek comment on the impact of such an approach on low-income subscribers.

271. We also seek comment on methods or arrangements for promoting more efficient use of analog channel capacity. Most video dialtone applications filed thus far propose to offer between 60 and 80 analog channels of video programming. In order to make more efficient use of this analog capacity, and to comply with our rules, four LECs have proposed "channel sharing arrangements."[509] The stated purpose of these analog channel sharing mechanisms is to maximize use of analog capacity by avoiding carriage of the same video programming on more than one analog channel, thereby making video dialtone more attractive and available to multiple video programmers, and more marketable to consumers. Generally, channel sharing arrangements would make available to all programmer-customers subscribing to the basic platform the programming on shared individual channels or blocks of channels. In turn, the shared channels could be made part of the programmers' general service offering.

272. While the various channel sharing proposals each have unique characteristics, they also share several features. Most of the plans provide for 10 to 15 "common" channels.[510] Generally, no programmer-customer would be required to purchase the common channels, although most LECs believe that it will be in programmer-customers' interest to use this service. According to the LECs, the shared analog channels will most likely carry off-air broadcast signals because under current market conditions, those are the most

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509 See Ameritech Operating Companies Section 214 application at 6 (Jan. 31, 1994); Ameritech ex parte statement, May 9, 1994, at 10-11; Bell Atlantic Section 214 application at 14 (June 16, 1994); Pacific Bell Section 214 application at 17 (Dec. 20, 1993); U S WEST Communications, Inc. ex parte letter, May 16, 1994, regarding Section 214 applications at Charts 1 and 2.

510 Bell Atlantic's "will-carry" proposal would provide as many as 37 channels for local broadcast and PEG programming. Bell Atlantic telephone companies Section 214 Application, File No. W-P-C-6966 at 4 (June 16, 1994); Bell Atlantic ex parte letter, July 1, 1994, at 9-12. See also, Bell Atlantic Section 214 Application, File No. W-P-C 6914 (June 16, 1994). See Third Further Notice, infra para. 284.

popular channels with consumers. Indeed, Pacific Bell's proposal would limit the use of shared channels to local off-air signals. Likewise, Bell Atlantic proposes to provide free carriage for local broadcast stations and PEG programmers seeking access.

273. The management of the shared channels varies among the proposals. Ameritech and Pacific Bell are similar in that they propose that a manager or administrator determine the programming for the common channels and secure the programming rights for those channels. US West takes a different approach, proposing that the programmer-customers work together to select the programming. US West would provide a "facilitator" to assist the programmer-customers, but would not maintain any long term involvement with such facilitator. The programmer-customers would be responsible individually for obtaining rights to the programming on the common channels. On the other hand, Bell Atlantic's proposal is broadcast-programmer driven, with local broadcast stations and PEG programmers requesting carriage, which Bell Atlantic would provide at no charge to the broadcaster or PEG programmers.

274. We tentatively conclude that channel sharing mechanisms, if properly structured, can offer significant benefits to consumers, programmer-customers, and video dialtone providers, while remaining consistent with the requirements of the cross-ownership provisions of the 1984 Cable Act. For example, these arrangements could increase the number of video programmers on the platform, thus creating diverse programming options. In addition, they would enable multiple video programmers to offer full service packages to consumers. Channel sharing arrangements would also maximize use of the platform by programmer-customers, thereby benefitting video dialtone providers.

275. At the same time, we recognize that, depending upon how they are structured, these arrangements can raise significant legal and policy issues. We therefore believe that the public interest would be well-served by the establishment of specific rules and policies to govern channel sharing arrangements. To this end, we now seek comment on the following issues: First, if channel sharing is permitted, who should structure or administer shared channels -- the LEC, a programmer-customer, a consortium of programmer-customers, or an independent third party? In this regard, we seek comment on the role that LECs may play in structuring or administering channel sharing arrangements without violating the cross-ownership provisions. If we conclude that video programmers should play a role in administering shared channel mechanisms, we propose to modify our rule prohibiting video programmers from jointly operating, with a LEC, a basic video dialtone platform. Second, what criteria should be used to select the shared channel administrator? Third, how should programming be selected for the shared channels? Fourth, we seek comment on the terms and conditions on which shared channels should be made available to programmer-customers. Finally, we seek comment on any

other relevant issue regarding channel sharing arrangements. We do not intend at this time to prescribe one kind of sharing arrangement, but to establish rules and policies that will ensure that any such arrangement will further the public interest and remain consistent with the 1984 Cable Act. Nor do we intend to defer consideration of Section 214 applications proposing channel sharing arrangements pending the development of rules and policies governing such arrangements. Rather, we will address those proposals on a case-by-case basis. Section 214 authorizations will, however, be conditioned on compliance with any subsequent rules that we adopt with respect to channel sharing mechanisms.

B. Modifications to our Prohibition on Acquisition of Cable Facilities

276. As discussed above, we have decided to retain our existing prohibition on the acquisition by telephone companies of cable facilities in their service area for provision of video dialtone. This ban, we believe, will further the public interest by promoting facilities-based competition for video services. Nevertheless, we have recognized that some markets may be incapable of supporting two video delivery systems. In these markets, our prohibition serves little useful purpose since facilities-based competition is not likely to develop or be sustainable in any event. Indeed, we are concerned that, in these markets, our prohibition would effectively preclude the establishment of video dialtone service, thereby denying consumers the benefits of a common carrier video transmission facility capable of serving multiple video programmers.

277. In light of these concerns, we now seek comment on appropriate modifications to our prohibition that would permit acquisitions of cable facilities in markets in which two wire-based multi-channel video delivery systems are not viable, while preserving the ban in other markets. Specifically, we seek comment on criteria that would permit us to identify those markets in which two wire-based multi-channel video delivery systems would likely not be viable.

278. We propose to amend our prohibition so that LECs would be permitted to purchase cable facilities in markets that meet these criteria. Alternatively, these criteria could serve as the basis for a presumption that a request for waiver of the prohibition would be granted. We tentatively conclude that LECs proposing to purchase cable facilities in their service area must identify the facilities to be purchased in their Section 214 application and demonstrate that the area served by those facilities meets the criteria we establish in this rulemaking. We seek comment on these proposals and on any other proposals parties might offer that would accomplish the same ends.

279. We also propose to amend our rules to permit LECs and cable operators jointly to construct a video dialtone system in those areas in which we permit LECs to acquire cable facilities for use in providing video dialtone. Permitting joint construction of video dialtone systems in such areas and shared costs of video dialtone might, in fact, encourage the deployment of advanced facilities in areas that otherwise might lack them. We seek comment on our proposal to permit joint construction of video dialtone systems in areas in which the acquisition ban is lifted.

C. Preferential Access Proposals

280. As discussed above, we have found that the record does not provide an adequate basis for deciding whether to mandate preferential video dialtone access or rates for certain classes of programmers, or whether to permit LECs voluntarily to provide preferential treatment to certain programmers. We now seek additional information and comment so that we may obtain a better factual basis for addressing these issues.

281. We seek comment, first, on whether we legally can, and should, mandate preferential video dialtone treatment for commercial broadcasters or for certain classes of PEG or not-for-profit video programmers. As noted above, we have authorized preferential treatment of certain classes of consumers when such treatment is justified by a compelling showing of need and public policy concerns. We invite parties to comment on whether there are public policy reasons to mandate preferential treatment for commercial broadcasters, or for certain types of PEG or not-for-profit programmers, such as, for example, noncommercial educational programmers. Parties addressing this issue should describe any such reasons with specificity, as well as the adequacy or inadequacy of alternative means of providing public support for such programmers, such as grants and direct subsidies. Parties should also address whether mandated preferences for certain types of programmers would be consistent with the First Amendment and the Supreme Court's decision in Turner v. FCC,[511] as well as with Title II of the Act, including Sections 201(b) and 202(a).[512]

282. We also invite parties to suggest a definition of the programmers they believe any such mandate should cover. Specifically, to the extent that any policy of preferential treatment would be based upon a finding of need, we seek comment on how such a policy could be fashioned to target not-for-profit video programmers most in need of preferential treatment. We also seek comment on appropriate affiliation rules that might be part of

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511 Turner Broadcasting System, Inc. v FCC, 114 S.Ct. 2445 (1994).

512 47 U.S.C. §§ 201(b), 202(a).

any such need-based test to ensure that video programmers that have certain affiliations with nonqualifying entities do not receive preferential treatment. In addition, we seek comment on whether preferential treatment should be available to any not-for-profit programmer meeting a means test or to only those programmers offering certain types of programming, such as educational programming. Parties should also address the First Amendment implications of any such classifications, as well as how such classifications would be administered. For example, parties should discuss whether a LEC role in determining eligibility of specific video programmers for preferential treatment would be consistent with the common carrier framework governing video dialtone, the cross-ownership provisions of the 1984 Cable Act, and relevant case law.

283. Finally, we seek comment on the type and amount of preference that should be mandated, in the event that we decide to prescribe preferential treatment for certain programmers. Parties should address, in particular, whether preferential access is necessary, or whether discounted rates alone would meet our public policy goals. Parties should also address how much of a preference should be granted. For example, parties advocating preferential rates should address how those rates should be calculated. We note that one possibility would be to base preferential rates on an incremental cost standard, whereby video programmers eligible for preferences would pay only for the incremental costs to the LEC of providing channel capacity to such programmers. We seek comment on this proposal and on any other proposal for implementing a preferential treatment policy.

284. We seek comment, second, on whether to permit LECs voluntarily to provide certain programmers with preferential treatment on LEC video dialtone platforms. For instance, in two of its video dialtone Section 214 applications, Bell Atlantic has proposed to reserve analog capacity for local broadcast stations, and PEG programmers, at no charge to these programmers.[513] We now seek comment on these "will carry" proposals. We also seek comment on whether we should permit LECs voluntarily to provide other forms of preferential treatment. For instance, should we permit LECs to offer preferential access or rates only to not-for-profit video programmers? Should we permit LECs to reserve capacity for local broadcast stations and PEG programmers at reduced rates? With respect to all proposals for voluntary LEC provision of preferential treatment, we seek comment on whether a permissive policy toward preferential access to video dialtone would be consistent with the First Amendment and the Supreme Court's decision in Turner v FCC. We also seek comment on whether these

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513 Bell Atlantic, File No. W-P-C 6966 (June 16, 1994) and Bell Atlantic, File No. W-P-C 6914 (June 16, 1994).

proposals would or could be consistent with Sections 201(b) and 202(a) of the Act, and, if so, under what circumstances. We invite comment as well on whether such proposals are consistent with the common carrier framework governing video dialtone, the 1984 Cable Act, and relevant case law, including NCTA v FCC. In addition, we seek comment, as we did above for mandatory preferential treatment, on all the issues entailed in identifying the categories of customers eligible for preferential treatment. Finally, we seek comment on whether these proposals, assuming they are lawful, would further the public interest.[514]

D. Pole Attachments and Conduit Rights

285. Section 63.57 of our rules requires LECs seeking to provide channel service to show in their Section 214 applications that the cable system for which the LECs would be providing channel service had available, within the limitations of technical feasibility, pole attachment rights or conduit space "at reasonable charges and without undue restrictions on the uses that may be made of the channel by the operator."[515] The rule seeks to prevent LECs from denying cable systems reasonable access to their pole or conduit space for the purpose of preventing competition from these cable systems.[516] We now seek comment on whether a similar rule should apply to LECs providing video dialtone service. Commenting parties should address whether LECs have the incentive and ability to leverage their control over pole attachments or conduit rights to prevent facilities-based competition by video programmers to the LECs' video dialtone platforms. Advocates of a rule in this area should propose specific language, and should explain how the rule would prevent anticompetitive behavior.

VI. CONCLUSION

286. For the reasons stated above, we conclude that the Second Report and Order, as modified herein, will eliminate artificial barriers to competition and distorted investment incentives and disincentives. This, in turn, will promote the public interest goals we have identified throughout this proceeding: facilitating competition in the provision of video

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514 Comments filed by parties in this proceeding will be transferred to the record of the Third Further Notice we issue today.

515 47 C.F.R. §63.57(1993).

516 See Applications of Telephone Companies for Section 214 Certificates for Channel Facilities Furnished to Affiliated Community Antenna Television Systems, 21 FCC 2d 307, 311, 314, 326-7 (1970), modified on recon., 22 FCC 2d 746 (1970).

services, encouraging deployment of the national telecommunications infrastructure, and fostering the availability to the American public of new and diverse sources of video programming.

VII. EX PARTE PRESENTATIONS

287. The Third Further Notice of Proposed Rulemaking is a non-restricted notice and comment rulemaking proceeding. Ex parte presentations are permitted, except during the Sunshine Agenda period, provided that they are disclosed as provided in the Commission's rules. See generally 47 C.F.R. §§ 1.1202, 1.1203 and 1.1206.

VIII. INITIAL REGULATORY FLEXIBILITY ANALYSIS

288. Pursuant to the Regulatory Flexibility Act of 1980, 5 U.S.C. §§ 601-612, the Commission's Initial Regulatory Flexibility Analysis with respect to the Third Further Notice of Proposed Rulemaking is as follows:

289. Reason for Action: The Commission is issuing this Third Further Notice of Proposed Rulemaking to consider whether to require or permit LECs providing video dialtone to grant preferential access or rates to certain classes of video programmers.

290. Objectives: The objective of the Third Further Notice of Proposed Rulemaking is to provide an opportunity for public comment and to provide a record for a Commission decision on the issues stated above.

291. Legal basis: The Third Further Notice of Proposed Rulemaking is adopted pursuant to Sections 1, 2, 4, 201-205, 215, 218, 220, and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152, 154, 201-205, 215, 218, 220 and 303(r); and 5 U.S.C. § 553.

292. Description, potential impact, and number of small entities affected: Amending our rules to require or permit LECs providing video dialtone to grant preferential access or rates to certain classes of video programmers may directly impact entities which are small business entities, as defined in Section 601(3) of the Regulatory Flexibility Act. Granting certain small video programmers preferential access to or rates on the video dialtone platform can have a positive impact on those entities by facilitating their provision of video programming to subscribers. On the other hand, preferential access or rates for certain small entities may negatively impact those small entities that do not receive preferential treatment. The Secretary shall send a copy of this Third Further Notice of Proposed Rulemaking to the Chief Counsel for Advocacy of the Small Business Administration in

accordance with paragraph 603(a) of the Regulatory Flexibility Act, Pub. L. No. 96-354, 94 Stat. 1164, 5 U.S.C. §601 et seq. (1981).

293. Reporting, recordkeeping and other compliance requirement: None.

294. Federal rules which overlap, duplicate or conflict with the Commission's proposal: None.

295. Any significant alternatives minimizing impact on small entities and consistent with state objectives: The Third Further Notice solicits comments on whether or not to mandate or permit preferential access or rates, as well as the types and extent of preferential access or rates that might be required or permitted.

296. Comments are solicited: Written comments are requested on this Initial Regulatory Flexibility Analysis. These comments must be filed in accordance with the same filing deadlines set for comments on the other issues in this Third Further Notice of Proposed Rulemaking, but they must have a separate and distinct heading designating them as responses to the Regulatory Flexibility Analysis. The Secretary shall send a copy of the Notice to the Chief Counsel for Advocacy of the Small Business Administration in accordance with Section 603(a) of the Regulatory Flexibility Act, 5 U.S.C. § 601, et seq..

IX. COMMENT FILING DATES

297. Pursuant to applicable procedures set forth in Sections 1.415 and 1.419 of the Commission's Rules, 47 C.F.R. §§ 1.415, 1.419, interested parties may file comments on or before December 16, 1994, and reply comments on or before January 17, 1995. To file formally in this proceeding, you must file an original and four copies of all comments, reply comments, and supporting comments. If you want each Commissioner to receive a personal copy of your comments, you must file an original plus nine copies. Comments and reply comments should be sent to Office of the Secretary, Federal Communications Commission, Washington, D.C. 20554. Parties should also file one copy of any documents filed in this docket with the Commission's copy contractor, ITS, Inc., Room 246, 1919 M Street, N.W., Washington, D.C. 20037. Comments and reply comments will be available for public inspection during regular business hours in the Dockets Reference Room of the Federal Communications Commission, 1919 M Street, N.W., Washington, D.C.

X. ORDERING CLAUSES

298. Accordingly, IT IS ORDERED that, pursuant to Sections 1, 4, 201-205, 214, and 220 of the Communications Act of 1934, as amended, and Section 613 of the Cable Communications Policy Act of 1984, 47 U.S.C. §§ 151, 154, 201-205, 214, 220, 533, the MEMORANDUM

OPINION AND ORDER ON RECONSIDERATION, affirming in part, and modifying in part, the SECOND REPORT AND ORDER in this proceeding, IS ADOPTED, as provided herein, effective 30 days after publication of a summary in the Federal Register, except that paragraphs 232, 243 and 244 shall be effective 90 days after publication of a summary in the Federal Register.

299. IT IS FURTHER ORDERED that the Petition for Rulemaking filed by CFA and NCTA is DENIED IN PART and GRANTED IN PART to the extent indicated above.

300. IT IS FURTHER ORDERED that, pursuant to Sections 1, 4, 201-205, 215, and 218 of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 154, 201-205, 215, 218, a THIRD FURTHER NOTICE OF PROPOSED RULEMAKING IS HEREBY ADOPTED.

301. IT IS FURTHER ORDERED that, the Secretary shall send a copy of this Third Further Notice of Proposed Rulemaking, including the regulatory flexibility certification, to the Chief Counsel for Advocacy of the Small Business Administration, in accordance with paragraph 603(a) of the Regulatory Flexibility Act, 5 U.S.C. §§ 601 et seq (1981).

FEDERAL COMMUNICATIONS COMMISSION

William F. Caton

William F. Caton
Acting Secretary

Appendix A: Parties Filing Comments
Reconsideration of the Second Report and Order
and Recommendation to Congress

Petitions for Reconsideration

ACT and Henry Geller (ACT)
Ameritech Operating Companies (Ameritech)
Association of America's Public Television Stations and Corporation for Public Broadcasting (APTS/CPB)
Association of Independent Television Stations, Inc. (INTV)
Bell Atlantic Telephone Companies (Bell Atlantic)
BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth)
California and the Public Utility Commission of California (California)
Consumer Federation of America and Center for Media Education (CFA/CME)
District of Columbia Public Service Commission
Florida Cable Television Association (FCTA) (filed late)
GTE Service Corporation (GTE)
National Association of Broadcasters (NAB)
National Association of Regulatory Utility Commissioners (NARUC)
National Cable Television Association, Inc. (NCTA)
New York City (NYC)
New York State Department of Public Service (NYDPS)
New York Telephone Company and New England Telephone and Telegraph Company (NYNEX)
Office of Communications of the United Church of Christ (OC/UCC)
Pacific Telesis Group, Pacific Bell and Nevada Bell (PacTel)
Pennsylvania Public Utility Commission (PaPUC)
Southwestern Bell Corporation (SWBT)
United Telephone Companies (UTC)
US WEST Communications, Inc. (US West)

Comments and Oppositions to Petitions

Ameritech Operating Companies (Ameritech)
Bell Atlantic Telephone Companies (Bell Atlantic)
BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth)
California Cable Television Association (CCTA)
Compuserve Incorporated (Compuserve)
Consumer Federation of America and Center for Media Education (CFA/CME)
Florida Cable Television Association (FCTA)
GTE Service Corporation (GTE)
Information Industry Association (IIA)
International Business Machines Corporation (IBM)
National Association of Broadcasters (NAB)
National Association of Telecommunications Officers and Advisors, the National League of Cities, the U.S. Conference of

Mayors, and the National Association of Counties (Coalition of Local Governments or CLG)
National Cable Television Association, Inc. (NCTA)
New England Cable Television Association (NECTA)
New York Telephone Company and New England Telephone and Telegraph Company (NYNEX)
Pacific Telesis Group, Pacific Bell and Nevada Bell (PacTel)
Pennsylvania Office of Consumer Advocate (PaOCA) (filed late)
Prodigy Services Company (Prodigy)
Southern New England Telephone Company (SNET)
Southwestern Bell Corporation (SWBT)
United States Telephone Association (USTA)
US WEST Communications, Inc. (US West)

Replies to Oppositions

America's Public Television Stations and Corporation for Public Broadcasting (APTS/CPB)
Ameritech Operating Companies (Ameritech)
Bell Atlantic Telephone Companies (Bell Atlantic)
District of Columbia Public Service Commission (DCPSC)
GTE Service Corporation (GTE)
National Cable Television Association, Inc. (NCTA)
New York Telephone Company and New England Telephone and Telegraph Company (NYNEX)
Pacific Telesis Group, Pacific Bell and Nevada Bell (PacTel)

Appendix B: Parties Filing Comments
CFA/NCTA Joint Petition for Rulemaking

Comments and Oppositions

American Telephone and Telegraph Company (AT&T)
Ameritech Operating Companies (Ameritech)
Association of Independent Television Stations, Inc. (INTV)
Bell Atlantic Telephone Companies (Bell Atlantic)
BellSouth Telecommunications, Inc. (BellSouth)
California and the Public Utilities Commission of the State of California (California)
California Cable Television Association (CCTA)
Citizens for a Sound Economy Foundation (CSEF)
District of Columbia Public Service Commission (DCPSC)
Edison Media Arts Consortium (Edison)
GTE Service Corporation (GTE)
Indiana Utility Regulatory Commission and the Michigan Public Service Commission (Indiana/Michigan)
National Association of Regulatory Utility Commissioners (NARUC)
National Association of State Utility Consumer Advocates (NASUCA)
National Telephone Cooperative Association (NTCA)
New Jersey Cable Television Association, Inc. (NJCTA)
NYNEX Telephone Companies (NYNEX)
Pacific Bell and Nevada Bell (PacTel)
Southern New England Telephone Company (SNET)
Telecommunications Industry Association (TIA)
United States Telephone Association (USTA)
US West Communications, Inc. (US West)
World Institute on Disability, the Consumer Interest Research Institute, Henry Geller and Barbara O'Connor (World Institute)

Reply Comments

Ameritech Operating Companies (Ameritech)
Bell Atlantic Telephone Companies (Bell Atlantic)
BellSouth Corporation and BellSouth Telecommunications, Inc. (BellSouth)
Broadband Technologies, Inc. (Broadband)
Consumer Federation of America and Center for Media Education (CFA/NCTA)
Compuserve Incorporated (Compuserve)
GTE Service Corporation (GTE)
New Jersey Board of Regulatory Commissioners (NJBRC)
New Jersey Cable Television Association (NJCTA)
New York Department of Public Service (NYDPS)
Organization for the Protection and Advancement of Small Telephone Companies (OPASTCO)
Pacific Telesis Group, Pacific Bell and Nevada Bell (PacTel)
R.G. Hale Consulting (Hale)
Telecommunications Industry Association (TIA)

United States Telephone Association (USTA)
US West Communications, Inc. (US West)

APPENDIX C: FINAL RULE CHANGES

Part 63 of Title 47 of the Code of Federal Regulations is amended as follows:

1. The authority citation for Part 63 is amended to read as follows:

AUTHORITY: Sections 1, 4(i), 4(j), 201-205, 218, and 403 of the Communications Act of 1934, as amended, and Section 613 of the Cable Communications Policy Act of 1984, 47 U.S.C. secs. 151, 154(i), 15(j), 201-205, 218, 403, and 533 unless otherwise noted.

2. Section 63.54 is amended to read as follows:

(a) [unchanged]

(b) [unchanged]

(c) [unchanged]

(d)(1) Except as provided in paragraph (d)(5) of this section, nothing in this section shall be construed to prohibit the provision of video dialtone services.

(2) Nothing in this section prohibits a telephone company from exceeding the carrier-user relationship with a video programmer or video programmers by providing services, and engaging in activities, not related to the provision of video programming directly to subscribers in its local exchange area.

(3) A telephone company may exceed the carrier-user relationship in its local exchange area with a video programmer by providing enhanced or other nonregulated services related to the provision of video programming to such video programmer, provided that a basic video platform is available to 70% of the households for which the video programmer seeks such enhanced or nonregulated services and provided that the telephone company does not:

(i) Determine how video programming is presented for sale to subscribers in its local exchange service area, including making decisions concerning the bundling or "tiering," or the price, terms, or conditions on which video programming is offered to subscribers in that area; or

(ii) Have a cognizable financial interest in, or exercise direct or indirect control over, any entity that performs any of the activities listed in paragraph (d)(3)(i) of this section within the telephone company's local exchange service area.

(4) A telephone company may exceed the carrier-user relationship with a video programmer or video programmers by

providing services, and engaging in activities, related to the provision of video programming (other than enhanced or other nonregulated services), provided that the telephone company does not:

(i) Determine how video programming is presented for sale to subscribers in its local exchange service area, including making decisions concerning the bundling or "tiering," or the price, terms, or conditions on which video programming is offered to subscribers in that area;

(ii) Have a cognizable financial interest in, or exercise direct or indirect control over, any entity that performs any of the activities listed in paragraph (d)(4)(i) of this section within the telephone company's local exchange service area;

(iii) Permit any video programmer to participate in the operation or management of basic video dialtone service, except as may be authorized by the Commission; or

(iv) Exceed the carrier-user relationship with any franchised cable operator in the telephone company's local exchange service area, or affiliate of such cable operator, except to: lease cable drop wires, in accordance with paragraph (d)(5) of this section, or to provide enhanced or other nonregulated services, in accordance with paragraph (d)(3) of this section.

(5) A telephone company may not acquire cable facilities in its local exchange service area for use in providing video dialtone service, or services related to the provision of video programming directly to subscribers. Notwithstanding the above, a telephone company may acquire cable facilities in its local exchange service area for use in providing common carrier channel service, subject to Section 214 certification and compliance with the Commission's rules. A telephone company may also lease drop wires from a franchised cable operator in its local exchange service area, provided that: (i) such lease is for a nonrenewable term of three years or less; and (ii) the telephone company does not obtain exclusive rights to use such drop wires, or otherwise unreasonably restrict the access of any video programmer to any of the cable operator's drop wires.

(e) In applying the provisions of this Section:

(1) [unchanged]

(2) [unchanged]

(3) [unchanged]

(4) [unchanged]

(5) Interests with rights of conversion to equity, including debt instruments, warrants, convertible debentures, and options, shall not be included in the determination of cognizable ownership interests unless and until conversion is effected.

(6) Attribution of ownership interests in a video programmer that are held indirectly by any party, other than an investment company, through one or more intervening entities, will be determined by successive multiplication of the ownership percentages for each link in the vertical ownership chain, and application of the relevant benchmark to the resulting product, except that wherever the ownership percentage for any link in the chain exceeds 50%, it shall not be included for purposes of this multiplication. (For example, if A owns 10% of company X, which owns 60% of company Y, which owns 25% of a video programmer, then X's interest in the video programmer would be 25% (the same as Y's interest since X's interest in Y exceeds 50%), and A's interest in the video programmer would be 2.5% (0.1 x 0.25)). Under the 5% attribution benchmark, X's interest in video programmer would be cognizable, while A's interest would not be cognizable. Paragraph (e)(2) of this section governs stock ownership interests held by an investment company in a corporation.

(f) Nothing in this section prohibits a telephone company from providing video programming directly to subscribers outside its telephone service area or from owning video programming that an unaffiliated video programmer directly provides to subscribers in the telephone company's service area.

(g) As used in this section, the term "video programmer" shall mean any entity that provides video programming either directly or indirectly through an affiliate, directly to subscribers. Any entity shall be deemed to "provide" video programming if it determines how video programming is presented for sale to subscribers, including making decisions concerning the bundling or "tiering," or the price, terms, or conditions on which video programming is offered to subscribers.

SEPARATE STATEMENT
OF
COMMISSIONER JAMES H. QUELLO

RE: VIDEO DIALTONE RECONSIDERATION ORDER AND THIRD FURTHER NOTICE OF PROPOSED RULEMAKING

The Commission's vote on video dialtone today is the culmination of our most painstaking consideration of the many complex legal, political, economic and technical issues that the construction of these advanced broadband communications systems presents. In the course of this deliberative process we have been required to address perhaps the most fundamental of telecommunications policy issues: what benefits will these systems bring, who will reap these benefits, short and long term, and who should pay for them. I am perfectly certain that not everyone will be perfectly satisfied that today's decision strikes the correct balances. So in my judgment the importance of what we do today calls for an explanation of why I, for one, am satisfied with these balances.

The issue of cost allocation has two dimensions: first, how to separate costs between the federal and state jurisdictions, and, second, how to apportion interstate costs between telephone ratepayers and the telephone company shareholders. On the federal-state separations issue, the question for me has never been one of whether the states should be involved in this cost apportionment process - for clearly they must be and they will be - but rather, how this involvement can most productively be realized. And in this regard, I am persuaded that the most productive way to provide a basis for federal and state regulators to make informed decisions is to first solicit the necessary data and other relevant information in a Notice of Inquiry. While the immediate convening of a federal-state joint board to review separations issues may have great facial appeal, the simple fact is, we do not yet have a body of data from which we believe any meaningful conclusions can be drawn at this time about the separations impact of building advanced telecommunications networks. Each of the pending video dialtone applications is, as our 1991 decision intended that they be, unique in certain material respects from all the others. Because of this, and given our limited experience in dealing with these applications to date, engaging the joint board process immediately would accomplish little of a concrete nature. Our Notice of Inquiry, on the other hand, is designed to compile precisely the kind of further information that could be meaningfully considered and evaluated by a joint board. For this reason, I support the Notice of Inquiry as a necessary predicate to convening a federal-state joint board to decide these issues.

On the issue of how interstate costs will be allocated between video dialtone and basic telephony, I do feel that the reconsideration item provides an approach that will allocate video dialtone costs in a fair and rational manner. Would changes to our generic cost allocation rules have accomplished

the same result? Yes. But the real question is, are changes to our cost accounting rules a necessary precondition to achieving the same result? And here, I think, the answer is no. Added to the detailed scrutiny we would normally provide in the course of the tariff review process are specific guidelines and filing requirements designed to highlight any misallocation of costs. In my judgment this approach should adequately safeguard the interests of telephone ratepayers as well as those of video dialtone's cable competitors. Moreover, should any legitimate issue of cost misallocation persist in an individual video dialtone tariff proceeding nothwithstanding these safeguards, I for one would not hesitate to provide interested parties a "fail-safe" defense in the form of granting access to the telephone company's underlying cost data pursuant to discovery authority under Section 403 of the Communications Act. For these reasons, and for purposes of proceeding at this point in time, I am satisfied with the approach the Commission elects today.

Finally, I should raise issues particularly close to my own public policy heart: whether broadcasters, commercial or noncommercial, should be granted free or reduced-rate access to carriage on video dialtone systems. Surely I give away no great secret when I say that, on a strictly policy level, such arrangements make eminent good sense to me. And yet I am sensitive to the need to develop as complete a record as we can on the on the decidedly complex legal and economic issues implicit in these initiatives. And so I look forward to reviewing in detail the comments filed in response to the questions we have posed in the Third Further Notice.

These are not, of course, the only difficult issues presented in the context of the video dialtone item we vote today. But with regard to all these issues, I cannot help but return to the observation, particularly true in complicated and controversial matters of public policy such as this, that the best is often the delayed enemy of the good. What we have in this item - although undoubtedly not the best to any single party interested in its outcome - is still a good, workable way of bringing the many benefits of video dialtone service to consumers in a fair and efficient way.

We have, for over a year, extolled the potential of the advanced information superhighway and the powerful and fundamental changes it can make in our everyday lives in the not-too-distant future. Video dialtone systems will constitute an important component - indeed, perhaps the first component - of that information superhighway to many people. It's time for the Commission to clear any remaining regulatory hurdles to the institution of video dialtone service that do not serve the public interest. In my judgment this reconsideration order does that, and it therefore has my support.

October 20, 1994

SEPARATE STATEMENT

OF

COMMISSIONER ANDREW C. BARRETT

RE: Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58 (CC Docket No. 87-266), and Amendments of Parts 32, 36, 61, 64, and 69 of the Commission's Rules to Establish and Implement Regulatory Procedures for Video Dialtone Service (RM-8221); Memorandum Opinion and Order on Reconsideration and Third Further Notice of Proposed Rulemaking

In this Order, the Commission considers petitions for reconsideration of the 1992 Second Report and Order, as well as a joint petition for rulemaking filed by the Consumer Federation of America and National Cable Television Association seeking cross-subsidy rules specific to video dialtone service. In completing the re-examination of the rules for video dialtone services, the Commission affirms the basic regulatory framework for video dialtone subject to certain modifications, and substantially denies the joint petition. The Commission also dismisses the use of an "anchor programmer" structure and issues a Third Further Notice of Proposed Rulemaking seeking additional information and comment on various issues, including various capacity issues, the treatment of must carry provisions, and a "will carry" preferential access proposal.

When the Commission adopted rules governing the implementation of video dialtone service in June 1992, I supported the action as a major step in the regulation of converging technologies.[1] At that time, the Commission was careful to balance the interest of allowing telephone companies to provide additional video services over their networks with the interests of those parties who were seeking to prevent the telephone companies from participating in any aspect of the video services market. My decision then was based on several principles for analyzing the issues raised by our review of the rules, including (1) establishing a regulatory framework that could provide incentives for additional facilities based competition for video programming services; (2) providing regulatory incentives for telephone company investment in network modernization; and (3) establishing a formal review framework for monitoring the various issues that will be addressed by Section 214 review of video dialtone proposals, such as cost allocation matters and potential discrimination issues.

While supporting the Order and Authorization granting the New Jersey Bell Telephone

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[1] See Telephone Company-Cable Television Cross-Ownership Rules, Sections 63.54-63.58 (CC Docket No. 87-266), Second Report and Order, Recommendation to Congress, and Second Further Notice of Proposed Rulemaking, 7 FCC Rcd 5781 (1992) (Separate Statement of Commissioner Andrew C. Barrett).

Company's Section 214 authority to construct, operate, own, and maintain facilities and equipment to provide video dialtone service in Dover Township, New Jersey -- the first such application to be granted -- I emphasized the importance of moving forward in authorizing video dialtone service in order to promote the significant public interest benefits that may be attainable through this new broadband service. My support for granting the authorization was premised on the understanding that we would need to continue to address the remaining fundamental concerns regarding the process of authorizing video dialtone services.[2] In particular, I was concerned that we needed to address the allocation of the costs among video services and other regulated voice services in greater detail at the tariff stage, and in the context of reconsideration.

I believe that the Commission's decision appropriately addresses the fundamental issues raised on reconsideration, especially with respect to the cost allocation concerns, by providing specific guidance regarding the identification of "direct costs" in the "new services test" for video dialtone tariffs. In viewing this decision on reconsideration, it is necessary to observe that the nature of competition in the multichannel video marketplace has fundamentally changed since the Commission issued its Second Report and Order on video dialtone in June of 1992, as the cable industry has become subject to pervasive regulation in significant aspects of its business, until incumbent cable operators become subject to "effective competition". As a result of this shift in the competitive and regulatory environment, the Commission's decision to continue along the path of authorizing video dialtone service is a fundamental step toward replacing the function of cable rate regulation with competitive constraints in the multichannel video marketplace. Despite the changes in the regulatory environment, I believe that the Commission's original goals for video dialtone service continue to guide us to move forward in authorizing the service in order to: (1) promote the development of an improved nationwide infrastructure, with broadband facilities extending to homes and businesses; (2) foster competition in the delivery of video and communications services; and (3) promote a diversity of information services. The changing regulatory environment, however, does focus attention on certain policy considerations regarding video dialtone, especially as we seek to provide regulatory parity for competing services.

With respect to the cost allocation issue, it is important to view the development of video dialtone service as a new broadband service, and not simply as a "new" service, because competing video services do exist. I also believe our regulatory approach must reflect the extent to which video dialtone service will constitute a truly incremental service, and identify where the components of the broadband network are common facilities for both voice and video service. Accordingly, the Commission's decision appropriately determines that existing rules, in conjunction with the tariff process, may provide a sufficient basis for identifying the direct costs of video dialtone service, while also providing a flexible mechanism for allocating the common costs to video and voice service that may be applied to individual video dialtone services. Furthermore, I am concerned that an attempt to establish "new" cost allocation rules to

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[2] See Order and Authorization, New Jersey Bell Telephone Company Video Dialtone Application (Dover Township, NJ), FCC 94-180, (released July 18, 1994) (Separate Statement of Commissioner Andrew C. Barrett).

accommodate this broadband service would further complicate the regulatory treatment of video dialtone service, without regard to the diverse networks that are developing to provide the service. As a policy matter, I believe the existing rules and new services test in the tariff process, along with the guidance provided in this decision, will provide a reasonable base to determine a price floor for video dialtone service, while providing the opportunity to gather and assess the information necessary to determine whether the results of this approach ultimately are producing a fair allocation.

I have been concerned, however, that the Commission's treatment of the cost allocation issues must address the policy concerns resulting from the competitive role of video dialtone relative to other multichannel distributors. This concern is heightened by the incentives and opportunities for LECs to establish a price for video service at a level that could cause an anticompetitive result due to cross-subsidies associated with voice services. To the extent that the process for identifying direct costs under the new services test in the tariff process will provide a measure of flexibility to telephone companies in reporting incremental costs and allocating the common costs of video and voice service, the policy concerns resulting from the development of video dialtone service might be exacerbated. I support this decision, however, because of the specific guidance developed to identify the elements of direct costs, including the incremental costs associated with plant dedicated to video dialtone service. In addition, it is important to emphasize that we have provided further guidance in defining the price floor for video dialtone service as we will expect LECs to include a reasonable allocation of other costs associated with shared plant used to provide video dialtone and other services in their estimation of direct costs, where such common costs exist. The use of the new services test also will maintain a measure of flexibility for LECs in allocating common costs provided that they follow a consistent and clearly delineated allocation process for other services. Therefore, this approach for cost allocation will avoid the inefficiencies of other possible allocators, such as cost- or revenue-based proportions, or a fixed allocation factor. In my estimation, none of these alternatives would realistically reflect a given LEC's practices or unique architecture for their broadband network for video dialtone service, and, thus, would mandate an artificial allocation scheme. In balancing the interests of continued steps toward authorizing video dialtone services with the need to establish a basis for determining an efficient and reasonable allocation of costs for that service, I emphasize that the determination of the cost allocation process and the pricing for video dialtone necessarily will be resolved during the 214 application and tariff process. These processes are intended to elicit and analyze much of the information required to establish an accurate cost and rate structure for any LEC service, including video dialtone.

Yet, I have been convinced for some time that the complexity of our costing and other procedures would not be able to cope with the far reaching changes in technology and market structures.[3] Indeed, I have stated that once the local exchange carriers are transporting broadband and video along with existing voice services, and wireless services are used

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[3] See "Beyond Price Caps: Escaping the Traditional Regulatory Framework", delivered by Commissioner Andrew C. Barrett to Florida Economic Club, August 27, 1992.

extensively for local access, the allocation of costs will have little meaning. The Commission's decision will create a new price cap basket for video dialtone service, and the combination of voice and video services will raise new policy concerns for the current price cap structure that maintains vestiges of rate-of-return regulation by requiring the allocation of costs among the LECs' respective services. I am concerned, therefore, that we will have to be consider the significant implications of this decision for the Commission's use and review of the LEC price cap mechanism, and I will be interested in how the Commission will address these questions related to the authorization of video dialtone service in the context of the LEC price cap review.[4]

This decision also opens an inquiry proceeding focusing on a concern of both federal and state regulators in terms of the implications for the jurisdictional separations process resulting from the introduction of new technologies, including broadband technology, into local exchange carrier networks. I support the effort to establish a dialogue between state and federal regulators on the fundamental questions related to cost treatment and the evolving nature of LEC networks. Given the complexity of these issues and the cost allocation results for video dialtone services in the tariff process, it will be important for both federal and state regulators to monitor the results of implementing regulatory procedures for video dialtone and work toward refining the jurisdictional separations process.

I also support the conclusion in this decision to dismiss proposals for "anchor programmer" structures by requiring LECs offering video dialtone to make available a basic common carrier platform with sufficient capacity to serve multiple video programmers, and may not provide all or substantially all of the video dialtone platform capacity to any one programmer. I am concerned that allowing video programmers such wide latitude to participate in the operation of the basic video dialtone platform would raise great risk of discrimination. To the extent that economic or marketing considerations would create incentives to rely primarily on a single programmer, I also am concerned that this result would be more consistent with "cable" service rather than the common carrier obligations under Title II of the Communications Act. I do believe, however, that channel sharing mechanisms, depending upon their structure, may offer significant benefits to customers, such that it will be useful to seek further comment to establish specific rules to govern channel sharing arrangements.

Finally, to the extent that this decision embodies a measure of flexibility for LECs, I will be interested in the Commission's actions to provide substantial flexibility to cable operators to augment the cable rate regulations through "going forward" provisions with clear incentives to add channels and to provide "a la carte" offerings. In addition, as the Commission develops final cost-of-service rules for cable systems to justify rates above the benchmark, it will be important for those standards to be compatible with the identification of direct costs and standards for allocating common costs in the video dialtone context. To that end, we must establish standards for allocating common costs for cable operators as they upgrade their distribution networks to

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[4] See Price Cap Performance Review for Local Exchange Carriers, CC Docket 94-1, NPRM (rel. Feb. 16, 1994), 9 F.C.C. Rec. 1687 (1994).

provide voice services.

Conclusion

Video dialtone will promote needed competition in the multichannel video services market, facilitate development of an advanced, national information infrastructure, and offer consumers more choices. While we seek to further telephone company participation in the video services market, we have taken care to craft a regulatory structure designed to protect consumers and competition alike. I will watch with anticipation and a careful eye as video dialtone develops, and will stand ready to make any necessary modifications to our rules.